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Supreme Court of the United States

OCTOBER TERM, 1945

No. 1143

WALTER P. GARDNER, Trustee of THE CENTRAL RAILROAD COMPANY OF NEW JERSEY,

A Debtor-Petitioner,

vs.

THE STATE OF NEW JERSEY,

Respondent.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

STATEMENT.

On August 14, 1944, the Trustees of the Debtor, in reorganization under Section 77 of the Bankruptcy Act, filed a petition entitled "Petition for Adjudication Concerning New Jersey State Tax Claims and for Order No. 250," which we shall hereinafter refer to as the petition of August 14 (T. pg. 55a). That petition prayed (T. pg. 79a):

> "that this Honorable Court, the premises considered, may promptly adjudicate (1) whether petitioners entered into a contract with the State of New Jersey, (2) whether such contract is binding on the parties

thereto, (3) whether, if not binding on the State, petitioners are nonetheless bound by the prejudicial actions taken by them, (4) if not binding on the parties thereto including petitioners, to what extent, if at all, the proofs of claim of the State of New Jersey should be allowed, (5) what order should in such event be made to restore the equivalent of the status quo ante as nearly as may be and (6) what in such event are the relative rights, claims, liens and priorities of the claimants in the assets of the Debtor's Estate; and that this Honorable Court may instruct petitioners whether to make on or before December 1, 1944 the additional payment on account of the taxes claimed and the additional interest payment required by Chapter 290 of the Laws of 1941, as amended by Chapter 241 of the Laws of 1942."

Conceiving that the Bankruptcy Court was wholly without jurisdiction to entertain such petition for the reason that (1) there is no power in the Bankruptcy Court summarily to review the matters and make the determinations or adjudications requested, and that, even if there were such power (2) the making of such determinations and adjudications concerning liens of the State affixed at the time of bankruptcy constitutes a suit against the State which may not be maintained without the State's consent, the State of New Jersey appeared specially and moved to dismiss the said petition on August 14.

The Bankruptcy Court's finding that the requisite jurisdiction did exist was reversed by the Circuit Court of Appeals as reported in *In re Central Railroad of New Jersey*, 152 F. (2d) 408. To understand the questions presently before this Court and in order to determine the applicability of the several sections of the Bankruptcy Act to the matters presently in controversy, a detailed statement of the prior litigation, which quite obviously impressed the Court below, is deemed necessary.

a. *Concerning the litigation with respect to the assessment of the* 1932 *to* 1939 *taxes.*

The current controversy concerning the assessment methods employed by the taxing authorities in the State of New Jersey actually began with the review of the 1931 assessments. The New Jersey Supreme Court denied a request for a reduction in the 1931 assessments in *Central Railroad Company of New Jersey* vs. *State Board of Tax Appeals*, 109 N. J. L. 395. The New Jersey Court of Errors and Appeals affirmed this judgment (112 N. J. L. 5) and certiorari was denied by this Court (293 U. S. 568). The 1931 taxes have been paid.

The Debtor appealed its 1932 assessment to the State Board of Tax Appeals. The assessment was affirmed after hearing. No application was made to the Supreme Court for a review of this judgment. The Debtor appealed its 1933 assessment to the State Board of Tax Appeals. This assessment was affirmed after hearing. The Debtor was then granted a review of the 1933 assessment by the New Jersey Supreme Court. On December 11, 1934, the Supreme Court affirmed the judgment of the State Board in *Central Railroad Company* vs. *Martin*, 114 N. J. L. 69. No appeal was taken to the New Jersey Court of Errors and Appeals, but instead this Debtor and certain other railroad companies brought suit in the United States District Court for the District of New Jersey, seeking a permanent injunction against the collection by the State of New Jersey of a portion of the taxes assessed against them for the years 1932 and 1933. The dismissal by the District Court of their application was affirmed by the Circuit Court of Appeals in *Lehigh Valley Railroad Company* vs. *Martin*, 100 F. (2d) 139, decided November 15, 1938. Application for certiorari was denied by this Court on April 19, 1939 (306 U. S. 651, rehearing denied 306 U. S. 669).

When the Attorney-General of New Jersey started proceedings to enforce the State's lien for taxes, the Debtor filed its petition under Section 77 of the Bankruptcy Act (T. pg. 57a).

Notwithstanding that all questions concerning the amount of the 1932 and 1933 taxes had been determined adversely to the Debtor and notwithstanding that the bankruptcy act gave power to the Trustees to borrow on trustees' certificates, in a market which this Court will judiciously notice could have been effected at a very low rate, the Trustees continued to resist the collection of the said taxes and allowed further interest to accumulate at 1% per month from October 30, 1939, down to and including the date that the present petition for certiorari was filed. (The Trustee since the filing of present petition for certiorari has made a substantial part payment on the tax debt, reserving all rights to continue litigation.)

Notwithstanding what had been said by the New Jersey Courts in the 1931 and 1933 cases, and again by the Court below with reference to the combined 1932 and 1933 cases, nevertheless this Debtor and other railroad companies appealed their 1934, 1935 and 1936 assessments to the State Board of Tax Appeals. No reviews of the judgments of the State Board for the years 1934, 1935 and 1936 were sought from the New Jersey Supreme Court in the manner provided by statute. On the contrary, the Debtor and the other railroad companies again resorted to the Federal Courts. The United States District Court entered a decree enjoining the collection of more than 60% of the 1934, 1935 and 1936 assessments until a revaluation of the property should be made by the State taxing authorities in conformity with the opinion of the said District Court. This was later increased to 70%. Upon appeal by the State, the judgment was reversed in *Central Railroad Company* vs. *Martin*, 115 F. (2d) 968, decided November 27, 1940. By their petition of August 14, the Trustees deny

that they were a party to the appeal before the United States Circuit Court of Appeals. Reference to the record in that case will show, however, that the Debtor did appear in the proceedings and that the injunction running against the State and to the said Debtor was dismissed. The mandate of the Circuit Court to the District Court specifically set aside the decree in favor of this Debtor. It is worthy of observation that counsel in the Circuit Court of Appeals' case was one of those whose name apears upon the present petition before this Court.

The present Debtor did not apply for certiorari to review this judgment. The New York, Susquehanna and Western Railroad Company, a party to the proceedings before the Circuit Court of Appeals and which is also under Section 77 bankruptcy proceedings, likewise did not seek certiorari. Judge Clark, who sat in the New York, Susquehanna and Western case, said with reference to further proceedings concerning such taxes, as reported in 38 Supp. 158, 160:

"We insist upon a proscription of futility."

All of the other railroad companies with the exception of the two just mentioned sought certiorari from this Court which was denied on April 28, 1941 (313 U. S. 568).

The Court below in reversing the judgment in the said case held that the question of the assessment method employed in connection with the 1934, 1935, and 1936 taxes had been made res adjudicata by *Central Railroad* vs. *Martin*, 114 N. J. L. 69, *supra*. We wish to emphasize that the United States Circuit Court of Appeals did not determine that legal questions concerning the assessing method used in arriving at the 1934, 1935 and 1936 taxes had been made res adjudicata by anything done below in those years, but on the contrary, held that all Federal questions had been made res adjudicata by the judgment of the New Jersey Supreme Court in connection with the 1933 assessments.

And again we call attention to the fact that notwithstanding what was said in that case, a large amount of 1934, 1935 and 1936 taxes were still due to the State of New Jersey at the time of the filing of the present petition for certiorari.

The Debtor and other railroad companies appealed their 1937 and 1938 assessments, which were at exactly the same level as the 1936 assessments, to the State Board of Tax Appeals. The two years were heard as a unit and an aggregate of 4,610 pages of testimony were taken and 450 exhibits were introduced into evidence. The assessments were affirmed by the State Board on May 13, 1941. Since the identical assessing method was employed, *Central Railroad* vs. *Martin*, 115 F. (2d) 968, *supra*, must be controlling and it must be the law of these latter years that all questions concerning the assessment method for such years had likewise been made res adjudicata by *Central Railroad* vs. *Martin*, 114 N. J. L. 69, *supra*. It was not the passage of the "Settlement Acts" which caused the railroads to refrain from again resorting to the certiorari procedure provided by our statutes or to the Federal Courts in the manner set forth above. They had exhausted every remedy that promised even a possibility of success and were confronted with the situation which caused the learned Judge in the *Susquehanna* case to make the classic remark concerning a "proscription of futility."

The Debtor appealed its 1939 assessment to the State Board of Tax Appeals. In that year the State Tax Commissioner made primary valuations substantially the same as those in 1938. On a review of the primary assessment provided by statute, the State Tax Commissioner made adjustments downward on water-front property. Appeals were taken from the final determination of the State Tax Commissioner by the Debtor seeking a further reduction and by the City of Jersey City seeking to have the assessments increased. The State Board of Tax Appeals dismissed the Debtor's appeal and restored the assessments

to the level of the 1938 assessments. The Trustees were notified of these decisions by letter dated June 15, 1942. Thereupon the Trustees obtained from the District Court an order upon the State taxing authorities and the Attorney-General to show cause why the judgment of the State Board of Tax Appeals should not be declared null and void. After hearing the District Court entered Order No. 171, whereby it was determined that the Debtor's tax liability for 1939 had been definitely fixed by Order No. 163, which had in turn fixed the assessment for 1939 at the lower level. This order was reversed by the United States Circuit Court of Appeals in *In re Central Railroad Company of New Jersey*, 136 F. (2d) 633, 640. An application for a writ of certiorari from this Court was denied (320 U. S. 805).

The above covers all of the tax years prior to bankruptcy. Notwithstanding the litigation set out above, all of which had been determined adversely to the Debtor, we find the amazing statement on page 8 of the petition for certiorari in this case that:

> "The taxes for the years 1934-1940, inclusive, were all in litigation before various administrative tribunals and courts."

The brief had reference to the time of the adoption of the first "Settlement Act" on July 22, 1941. It is this thorough lack of appreciation of the effect of the above-mentioned judgments that has given rise to these present proceedings whereby the Trustees of the Debtor again seek to litigate matters long since declared by courts of competent jurisdiction to have been res adjudicata.

b. *Concerning the Tax Settlement Acts litigation.*

As we have stated, notwithstanding the successful termination of the litigation for the tax years 1932 to 1936, all adversely to the claims of the railroad companies, large amounts of taxes for those years still remained unpaid in July, 1941. The Legislature of the State of New Jersey, in a spirit of desperation brought about by the concerted refusal of the railroad companies to pay millions of dollars in taxes due and payable to the State of New Jersey, adopted Chapter 290 of the Laws of 1941, whereby it was sought to forgive the several railroad companies their obligation to pay back interest and to permit the payment of the principal amount of the taxes over a period of years plus 3% interest on the unpaid balance. This Act and Chapter 241 of the Laws of 1942, which is amendatory thereof, are designated as the "Tax Settlement Acts."

The 1941 Act provided in Sections 7 and 8, as set forth on page 7 of the Petition for Certiorari, for the participation by the Attorney-General in the tax settlement scheme. The Attorney-General being of the mind that the Act was unconstitutional refused to give his consent and instead on September 4, 1941, (barely six weeks after the passage of the Act), filed an information in the Court of Chancery of New Jersey seeking a determination as to the constitutionality of the said Settlement Act.

The railroad companies seeking to obtain the benefits afforded by the said Act, regardless of the refusal of the Attorney-General to participate in the settlement machinery, discontinued certain pending further appeals of their 1937 and 1938 taxes. From the above it can be seen that such discontinuance was a matter of form only as there was no meritorious questions left to be litigated. As was said in *Wilentz* vs. *Hendrickson*, 135 N. J. Eq. 244, 260, with respect to this very litigation:

> "• • • the asserted rights of the railroad taxpayers are 'illusory,' rather than real."

Be that as it may a reading of the Act discloses that there was no necessity of discontinuing these suits. It was only required that discontinuance documents be filed with the fiscal officers of the State which would have been returned just the same as the purported tenders of the railroads had to be returned upon the determination that the Acts were unconstitutional.

Notwithstanding that the several railroad companies did not seek to intervene in the tax settlement controversy and were not parties to such litigation, the record discloses that the matter was strongly litigated, the Attorney-General on the one hand urging the unconstitutionality of the Acts and the State Treasurer on the other, through eminent counsel, urging the constitutionality of such Acts. Not only this but the Legislature of New Jersey sought to cure obvious constitutional deficiencies by the adoption of the amendatory act in May, 1942 (Chapter 241 of the Laws of 1942) during the pendency of such litigation.

On May 21, the very day the amendatory act was enacted into law, under which the participation of the Attorney-General was eliminated, an injunction issued out of the New Jersey Court of Chancery restraining the State fiscal officers from accepting any payment or otherwise performing the terms of the Settlement Acts. On July 20, 1943, the Court of Chancery determined the Settlement Acts to be unconstitutional (*Wilentz* vs. *Hendrickson*, 133 N. J. Eq. 447). The New Jersey Court of Errors and Appeals affirmed the decree of the Chancery Court on June 22, 1944. (135 N. J. Eq. 244.)

In the meantime and on June 2, 1942, the Trustees petitioned the District Court for instructions with reference to their compliance with the Settlement Acts. As a result of such petition, the Trustees were instructed and directed to comply with the said Settlement Acts and Order No. 163 was entered fixing the amount due to the State of New Jersey for taxes and interest at the amount that was provided

by the terms of the said Acts. The State of New Jersey appealed to the United States Circuit Court of Appeals for the Third Circuit. On May 27, 1943, the said Court reversed the said Order No. 163 and held that the District Court in the exercise of a nice discretion should have withheld any determination as to the constitutionality of the Settlement Acts pending the determination by the New Jersey Courts of such questions (136 F. 2nd 633). It is significant that the Circuit Court of Appeals made its determination prior to the judgment by the New Jersey Court of Chancery and in plenty of time for the Trustees to have applied to intervene in the New Jersey Settlement Acts litigation. A re-hearing was denied on July 15, 1943, still prior to July 20, 1943, the date of the judgment by the Chancery Court. It should likewise be pointed out that the Trustees had more than one year from May 27, 1943, until June 22, 1944, when the Court of Errors and Appeals made its final determination within which to intervene in the Settlement Acts' controversy.

The Trustees by their petition of August 14, now seek to have the Bankruptcy Court make an adjudication that a binding contract exists with the State of New Jersey upon the basis of their abortive attempts to comply with the terms of the unconstitutional Settlement Acts. This contention was disposed of adversely to the Trustees in *In re Central Railroad Company of New Jersey*, 136 F. (2d) 633, 638, *supra*, wherein the Court said:

> "The final contention that the issue between the State and the Trustees is moot by reason of the tender to the Treasurer of a payment pursuant to Order No. 163 must also fail. The tender though acknowledged was not accepted by the Treasurer and consequently was without legal effect. In fact, the Treasurer was powerless to accept the tender by reason of the injunction issued by the Court of Chancery.",

The very same argument that is now advanced by the Trustees in connection with the present application was advanced before this Court in connection with an application for a writ of certiorari to review the judgment in the just mentioned case, which application was denied. (320 U. S. 805.)

c. *Concerning the litigation on the August 14 petition.*

As stated above, approximately two months after the New Jersey Court of Errors and Appeals made its determination in *Wilentz* vs. *Hendrickson, supra,* the Trustees filed its petition of August 14, wherein the Trustees sought to have the Bankruptcy Court make certain determinations with respect to the taxes and interest due to the State of New Jersey, as more particularly set forth on page 1 above.

The Trustees have set forth on page 2 of their petition "the essential questions" which must be determined. It is apparent from a reading of the petition of August 14, and the present petition that the Trustees still seek to have the Bankruptcy Court make a re-determination of the questions decided adversely to themselves in *Wilentz* vs. *Hendrickson, supra,* and in *In re Central Railroad Company of New Jersey, supra.* It is also quite apparent that the Trustees sought by the petition of August 14, to have the Bankruptcy Court re-determine certain tax questions which had been said by the Federal Courts to have been made res adjudicata by the New Jersey Supreme Court in *Central Railroad Company* vs. *Martin,* 114 N. J. L. 69, *supra.* They have requested the Bankruptcy Court to make certain other adjudications but have not shown where the Bankruptcy Act has given jurisdiction to the Court in such matters.

Since all of the taxes due to the State of New Jersey had become a lien paramount to all other liens upon the lands, tangible property and franchises in the State of New Jersey, not later than June 1, 1939, and over four months prior

to October 30, 1939, when the petition in bankruptcy was filed, the State moved on special appearance to have itself dismissed as a party to the said petition insofar as it was sought to take jurisdiction for the purpose of making adjudications that would be binding upon the State of New Jersey with respect to the tax liens of the said State. The argument of the State concerning the jurisdiction of the Bankruptcy Court was comprised within two broad classifications (1) Congress did not give power to the Bankruptcy Court to undertake the review sought by the Trustees in the instant case; and (2) if Congress intended to grant such power in a case such as this, such grant of power is unconstitutional in that it violates the right of the State to be immune from suit in any court of the United States unless the State consents thereto.

Over objection of the State, the District Court Judge referred the matter contained in the petition of August 14, including the jurisdictional questions to the Standing Master for determination and report. The Standing Master made a finding that the Bankruptcy Court did have jurisdiction to entertain the several matters contained in the said petition. Again, over objection of the State, the District Court Judge confirmed the report of the Standing Master by its Order No. 271.

The Court below, in reversing this order, held that it was not necessary to answer the jurisdictional objections set forth in the two broad classifications above because the jurisdiction of the Bankruptcy Court was limited in the manner set forth in *Arkansas Corporation Commission* vs. *Thompson*, 313 U. S. 132. It held, in effect, that even if there is jurisdiction, yet under the facts of the instant case such jurisdiction is limited to a determination of whether there was mathematical error in computation. The Court said that:

"Failure of this opinion to touch upon certain points raised by the State of New Jersey is not to be construed as meaning that they are without merit; rather, our decision renders discussion of them unnecessary."

The Court thereupon reversed Order No. 271 with costs to the State and stated that since this disposed of the entire matter before them the application for the writ of prohibition should be dismissed without costs to either party.

d. *Concerning the present petition of the Trustee.*

Several matters contained in the petition and brief of the Trustee require denial or clarification in this statement rather than in the argument:

1. The Trustee's statement (Pet. pg. 10) that the Trustees had fully complied with the terms of the Railroad Tax Settlement Acts is contrary to the law of this case as determined in *In re Central Railroad Company of New Jersey*, 136 F. (2d) 633, 638 (5).

2. The Trustees' insistence that the 1934-1940, inclusive, taxes (Pet. pg. 8) were still in litigation on July 22, 1941, is without any support in fact. *Central Railroad* vs. *Martin*, 115 F. (2d) 968, *supra*, is completely dispositive of this contention.

3. The Trustees' contention that they were required to discontinue the alleged appeals is without foundation in fact. They were simply required to comply with the terms of the Settlement Acts as set forth on page 7 of the Trustees' petition, a reference to which will show that a tender of the required documents would have been a compliance in the same manner as their attempted compliance by tendering the several payments required by the terms of the Act. Had the Acts been declared to be constitutional, this would have been compliance with said terms. The Courts upon application would have permitted a continuance of pending litigation during the time needed to determine the constitutional question.

4. The Trustees' assertion that the denial of the State's petition for a writ of prohibition is not before this Court is without merit. The Court below on its own motion consolidated the argument on the two cases in order that the jurisdictional questions would be before the Court. A disagreement with the Court below concerning the limits of the Court's jurisdiction under the *Arkansas Corporation Commission* case could result in this Court's arriving at the same result but for different reasons on the basis of the full record in the Court below.

5. The State by its claim filed in this cause gave notice to the Bankruptcy Court that it had a lien for its 1932 to 1939 taxes under the appropriate New Jersey statutory provisions and laid the basis for a claim against the unsecured assets of the Debtor in the event that the security afforded by the statute should be insufficient to pay the amount of tax and interest due to the said State.

6. The Trustees (Pet. pg. 17) cites the case of *Hyman* vs. *Long Branch Kennel Club*, 115 N. J. L. 123, in support of the premise that the Trustee could obtain rights under the Settlement Acts prior to the determination by the Courts of the State of New Jersey that such acts were unconstitutional: The *Hyman* case is authority for just the contrary doctrine. The said case is authority for the rule that an unconstitutional statute is void from the beginning.

7. On page 10 of the petition, the Trustees state that they do not now contend they are entitled to a reduction in the principal amount of the taxes as assessed. A reading of that paragraph discloses that the Trustees do not come to such conclusion because of the great amount of litigation which has resulted adversely to themselves in connection with such taxes, but they rely upon the premise that the amount has been settled by reason of their compliance with the Tax Settlement Acts, a question already determined adversely to themselves in *In re Central Railroad Company of New Jersey*, 136 F. (2d) 633, *supra*, wherein Orders No. 163 and No. 171 were reversed.

SUMMARY OF ARGUMENT.

The Trustees have petitioned this Court for a writ of certiorari to review a judgment of the Third Circuit reversing an order of the Bankruptcy Court whereby the said Bankruptcy Court determined that it had jurisdiction to make certain adjudications requested by the Trustees in the petition of August 14. The Trustees have failed to show in what respect the said order of reversal has done violence to any authoritative pronouncement of this Court. This lack is quite understandable since, with respect to two of the only three important questions presented by the said petition, this Court has spoken with definiteness and finality in *Arkansas Corporation Commission* vs. *Thompson*, 313 U. S. 132, and *Meilink* vs. *Unemployment Reserves Commission*, 314 U. S. 564. The third question was before the Third Circuit in *Central Railroad Company of New Jersey*, 136 Fed. (2d) 633, wherein the said Court reversed Order No. 163 of the Bankruptcy Court in these proceedings, which Order sought to do exactly what the Trustees hope to accomplish by the petition of August 14. (Cert. den. 320 U. S. 805.)

The Trustees in the Court below urged that Section 64 gave power to the Bankruptcy Court to make the requested adjudications. In our first point we show the limits of the power contained in Section 64 as determined by this Court in the said *Arkansas Corporation Commission* case. We will argue that, on the facts of this case, the power of the Bankruptcy Court was so limited that it was, in fact, wholly without power to consider one single prayer.

While we believe with the Court below that this determination by this Court is dispositive of the whole matter, nevertheless we have considered at length the other two questions. In Point II we deal with the former attempt of the Trustees to have the Bankruptcy Court fix the liability

of the Trustees at the amount prescribed by the Settlement Acts. The Court there had before it the very same argument concerning the existence of a contract and disposed of this contention adversely to the Trustees. As we show in our Point II the determination by the New Jersey Court of Errors and Appeals in *Wilentz* vs. *Hendrickson*, 135 N. J. Eq. 244, is dispositive of the other questions urged by the Trustees in this connection.

In Point III we deal with the power of the Bankruptcy Court to denominate as a penalty that which by State statute is stated to be interest. This case is clearly within the rule laid down by this Court in *Meilink* vs. *Unemployment Reserves Commission, supra,* wherein it was held in construing almost identical language that the Bankruptcy Court must treat the amount as interest and was, therefore, given no authority under Section 77 to reduce the amount.

In Point IV we point out that an argument advanced by the Trustees for the first time here with reference to the change in the law in 1941 is without merit.

Since we firmly believe that, had the Court below not followed the reasoning of the *Arkansas Corporation Commission* case, it still must have concluded that the Bankruptcy Court was, for certain reasons stated in the argument below, without power to make the requested adjudications concerning the tax liens of the State of New Jersey affixed at the time of bankruptcy and that, in case of a review, the result must be the same although perhaps such result might be based upon other grounds, we pray the indulgence of this Court in presenting at this time in our Point V an abbreviated version of our unanswered argument below concerning lack of jurisdiction under the following subpoints: (a) Section 64 does not authorize the Bankruptcy Court to make the requested adjudications; (b) Section 77 does not give such power; (c) Section 67 does not give such power; (d) since the liens of the State were affixed prior to bankruptcy, the Bankruptcy Court may not

make adjudications to be binding upon the State of New Jersey without the State's consent; and (e) the State of New Jersey has not consented to the making of such adjudications.

From the above, we shall urge that the petitioner has not shown a case warranting the issuance of the discretionary writ of certiorari.

ARGUMENT.

POINT I.

The Court below applied the applicable rule of law as set forth in *Arkansas Corporation Commission* vs. *Thompson*, 313 U. S. 132.

The Trustees by their petition of August 14, sought to have the Bankruptcy Court in a summary manner make adjudications concerning the several matters set forth in detail at page one of this brief and involving three broad questions: (1) the power of the Bankruptcy Court to adjudicate concerning the constitutionality and applicability of the "Settlement Acts"; (2) the power of the said Court to reduce the interest rate; and (3) the power of the said Court to re-determine the amount of the assessments.

But where in the Bankruptcy Act can we find the power in the Bankruptcy Court to make such adjudications in a summary manner? The Trustees urged below that Section 64 gives the said Court such power. Reference to the interim report of the standing master (T. pg. 163a) discloses that the Master found the power to make the said adjudications in the said Section 64.

As we will show in detail hereafter, it has been uniformly held that Section 64 does not apply to secured claims but only to unsecured claims, to those claims which but for the priorities given in the said section would have no priority

and would share only in the residual estate available for general creditors. Likewise there has been considerable doubt whether Section 64 applies in railroad reorganization proceedings under Section 77 in any event.

This problem was before this Court, although in a matter involving taxes accruing during bankruptcy, in *Arkansas Corporation Commission* vs. *Thompson*, 313 U. S. 132. In that case, which should be dispositive of the matter presently before this Court, this Court said that it was unnecessary to decide whether Section 64 applies in Section 77 proceedings because, conceding the applicability of the said Section 64, the Bankruptcy Court was still without jurisdiction to review the disputed tax assessments since an adequate judicial review was afforded by the laws of the taxing State. This Court held that the Bankruptcy Court should have dismissed the petition.

The Circuit Court of Appeals below construed the *Arkansas Corporation Commission* case in *In re Monongahela Rye Liquors*, 141 F. (2d) 864. The majority of the Court held that, where a judicial review of assessments is afforded by the local law, the Bankruptcy Court is limited to review for the purpose of (1) examining for mathematical error in the computation of the tax, or (2) legal error in the assessment. In an opinion which concurred in the result, Judge Biggs refused to apply the rule of the *Arkansas Corporation Commission* case but held instead that the facts of the *Monongahela Rye Liquors* case brought it within the rule of *New Jersey* vs. *Anderson*, 203 U. S. 483, which latter case was distinguished by this Court in the *Arkansas Corporation Commission* case.

It is difficult to read into the last mentioned case the exact construction placed upon it in the *Monongahela* case for the reason that this Court said in the former case that the question of the legality of taxing laws would in the orderly course of events come before the Federal Court by way of review of the judgments of the State Court of last

resort. However, it is unnecessary to decide this question because Judge McLaughlin below in applying the rule of *Arkansas Corporation Commission* vs. *Thompson, supra,* as construed by the *Monongahela* case, applied a further factor, the determinations by the Third Circuit, adversely to the Trustees' debtor, in *Lehigh Valley* vs. *Martin,* 100 F. (2d) 139, *supra,* and *Central Railroad* vs. *Martin,* 115 F. (2d) 968, *supra,* which dealt with the legality of the assessments. This, of course, eliminated the second portion of the above mentioned rule of the *Monongahela* case and left only the power to review for mathematical error in computation.

The Court below did not pass upon the several questions raised by the State concerning the applicability of the several sections of the Bankruptcy Act to the tax liens of the State affixed prior to bankruptcy and concerning the State's right to be immune from suit with respect to such liens unless the State consents for the reason that the determination of such questions were deemed by the Court to be wholly unnecessary.

Just as this Court in the *Arkansas Corporation Commission* case said that it was unnecessary to determine whether or not Section 64 applied to Section 77 reorganization proceedings for the reason set forth therein, so Judge McLaughlin in effect said that it is unnecessary to determine the applicability of Sections 64 and 77 to liens which were affixed at the time of bankruptcy or to determine the question of whether or not the present petition in fact constituted the institution of a suit against the State, for the reason that, conceding that all of these questions should be decided adversely to the State of New Jersey, yet the Bankruptcy Court under the facts and law of the instant case only had power to review the assessments made by the State of New Jersey to determine whether or not there was mathematical error in the computations.

As was obviously recognized by the Court below, our case is even stronger than the *Arkansas Corporation Commission* case because the debtor herein actually had litigated in the State and Federal Courts all questions concerning the legality of the New Jersey taxing methods. In the said case, at page 144, this Court said:

> "If the trustee had availed himself of his right of appeal to the courts of Arkansas, with an ultimate right of appeal to this Court for final determination of federal questions, it is difficult to believe that it would now be seriously argued that Congress, by § 64 (a) (4), intended to impose upon the bankruptcy court the unusual power and delicate duty of trying out afresh the facts found by the state with relation to the value of property. And there is no more reason to assume that Congress intended that the bankruptcy court should fail to give respect to an unappealed determination of value made by the Arkansas Corporation Commission."

The present case involves a factual situation similar to that suggested by this Court in the above statement as being difficult of belief. It is wholly inconceivable that anyone may now seriously contend that, in the light of the litigation that has gone before concerning the 1932-1939 taxes of the debtor, there exists in any court a right to review the New Jersey tax assessments for such years. It seems obvious that the Trustees by their petition of August 14, with its welter of conflicting matters, claims and complaints, have sought, under the guise of a review of the tax assessments, actually to obtain in a summary manner in the Bankruptcy Court a review of a determination by the New Jersey Court of Errors and Appeals that the so-called Settlement Acts are unconstitutional and an adjudication

on the question whether, notwithstanding such unconstitutionality, this debtor may still avail itself of certain benefits intended to be afforded by such acts.

It appearing therefore that the jurisdiction of the Bankruptcy Court in our particular case extends only to a determination whether there is mathematical error in computation, we ask ourselves the following: Does the answer to the first prayer contained in the petition of August 14, concerning the existence of a contract with the State of New Jersey, involve the determination of such mathematical error? The answer is obviously in the negative. And so with each of the other prayers contained in the said petition. Not one concerns itself with the determination of mathematical error. It follows therefore that the Bankruptcy Court improperly assumed jurisdiction with respect to the several matters sought to be adjudicated in the said petition for adjudication, and the Court below following the rule laid down in *Arkansas Corporation Commission* vs. *Thompson, supra,* quite properly reversed the judgment of the lower Court.

POINT II.

Regardless of the rule of *Arkansas Corporation Commission* vs. *Thompson, supra,* the Bankruptcy Court was required to follow *In re Central Railroad Company of New Jersey,* 136 Federal (2d) 633, *supra,* with respect to the applicability of the Settlement Acts and so was without jurisdiction to make the adjudications requested by the Petition of August 14.

As stated above, the New Jersey Legislature sought to forgive certain railroad companies the payment of interest due to the State on account of default in payment of railroad taxes in the years 1932 to 1940, inclusive. By Chapter 291 of the Laws of 1941, provision was made for the approval of the Attorney-General to certain documents required in order to accomplish a settlement under the

terms of the said Act. Conceiving the said Act to be unconstitutional, the Attorney-General refused to participate in the settlement procedure but instead, on September 4, 1941 (barely six weeks after the passage of the Act), filed an information in the New Jersey Chancery Court in order to obtain a determination as to the constitutionality of the said Settlement Act.

On May 21, 1942, the New Jersey Legislature amended the 1941 Act to provide a settlement procedure which did not require the participation of the Attorney-General, this notwithstanding the pendency of the just mentioned litigation (Chapter 241 of the Laws of 1942). On the very same day that the amendatory act was passed, the New Jersey Chancery Court issued its injunction prohibiting the fiscal officers of the State from accepting any money or tender pursuant to the terms of the Settlement Acts pending the determination of the constitutional question. On July 20, 1943, the Settlement Acts were held unconstitutional in *Wilentz* vs. *Hendrickson*, 133 N. J. Eq. 447. This judgment was affirmed by the New Jersey Court of Errors and Appeals on June 22, 1944 (135 N. J. Eq. 244). The injunction was thereupon made permanent.

In the meantime and about June 2, 1942, the Trustees for the Debtor filed a petition with the Bankruptcy Court requesting instructions concerning the acceptance of the terms of the Settlement Acts and requesting that an order be entered fixing the amount due to the State of New Jersey on account of taxes due for the years 1932 to 1940. The Bankruptcy Court by its Order No. 163 proceeded to determine that there was due to the State of New Jersey on account of the said tax obligation only that amount of money required under the terms of the Settlement Acts, this notwithstanding that the said Settlement Acts were presently in litigation and the fiscal officers of the State were restrained from accepting any moneys or documents pursuant to the terms of the said Acts. The Circuit Court

of Appeals below reversed the said order in *In re Central Railroad Company of New Jersey*, 136 Fed. (2d) 633, *supra*, holding that:

> "It would, therefore, have been appropriate, in the exercise of a wise discretion for the District Court to have staid its hand until the State Court had determined whether the Tax Settlement Acts were valid or a nullity."

The Trustees' application for a writ of certiorari to review this determination was denied by this Court (320 U. S. 805).

In the course of the just mentioned controversy, the Trustees advanced the same arguments which they are presently using to support their allegation that the Settlement Acts are binding as to them. They urged that there was a binding contract between the State of New Jersey and themselves and that they had fully performed. The conclusion of the Court below on this matter is set forth at page 638 of the just mentioned opinion as follows:

> "The final contention that the issue between the State and the Trustees is moot by reason of the tender to the Treasurer of a payment pursuant to Order No. 163 must also fail. The tender though acknowledged was not accepted by the Treasurer and consequently was without legal effect. In fact the Treasurer was powerless to accept the tenders by reason of the injunction issued by the Court of Chancery."

It is inconceivable that the Circuit Court of Appeals could have intended that the District Court should have, in the exercise of a nice discretion, waited to learn the views of the New Jersey Court on the question of constitutionality, unless the said Circuit Court of Appeals intended, since only the construction of a State statute was involved, that the District Court would be bound by the result. It is

wholly illogical that it could have intended that the said District Court would have been bound only if the matter were determined in favor of the Trustees and adversely to the State of New Jersey.

The case of *Wilentz* vs. *Hendrickson*, 135 N. J. Eq. 244, *supra*, was fairly litigated and the said litigation covered the railroad taxes of all the defaulting railroad companies, including the present Trustees. Of particular significance is the fact that the New Jersey Legislature sought vainly to remedy certain obvious unconstitutional defects in order to assist the defaulting railroad companies.

In this connection it should be pointed out that the Trustees stood by while the said litigation was pending and made no effort to be heard therein. This attitude continued even after they had learned the view of the United States Circuit Court of Appeals as expressed in *In re Central Railroad Company of New Jersey*, 136 Fed. (2d) 633, *supra*, at a time when there was still ample time to have intervened in the argument before the New Jersey Court of Errors and Appeals. Also it must be remembered that equitable principles prevail in the application of the provisions of the Bankruptcy Law. Equity favors the diligent and looks with disfavor upon one who withholds his action in the hope that by his own inaction he may obtain a sharp advantage. The Trustees were aware of every step that was being taken in the course of that litigation and can not be heard to complain now on the score that the result might have been different had they seen fit to intervene.

The Trustees have pointed to no provision of the Bankruptcy Act which gives the Bankruptcy Court the power summarily to relitigate the subject matter of the controversy presented by *Wilentz* vs. *Hendrickson*, *supra*, and by in *In re Central Railroad Company of New Jersey*, 136 Fed. (2d) 633, *supra*. The Court below quite properly refused to find jurisdiction in the Bankruptcy Court to make the requested adjudications concerning the Settlement Acts.

The Trustees have shown no compelling reason why this Court should issue its discretionary writ of certiorari for the purpose of reviewing this particular phase of the matter upon which the Trustees seem to place such stress.

POINT III.

Regardless of the rule of *Arkansas Corporation Commission* vs. *Thompson*, the Bankruptcy Court was bound by the rule established by this Court in *Meilink* vs. *Unemployment Reserves Commission*, 314 U. S. 564, denying jurisdiction in the Bankruptcy Court to define as a penalty that denominated as interest under State law in order to apply section 57.

The Trustees in their present petition (Pet. pg. 14) state,

> "Incidental questions arise whether, because of the facts and circumstances of this case the Bankruptcy Court should not in any event exercise its equity jurisdiction to do equity (Section 77 (A) and Section 2-a of the Bankruptcy Act), by determining that in no event should the State's claim carry penalty interest at 1% per month * * *."

The Trustees can gain nothing by designating the interest charged by the State of New Jersey as penalty. There can be no doubt but that the charge is interest under the decisions of this Court. It is provided in Section 57 that debts owing to the United States or any State or subdivision thereof as a penalty or forfeiture shall not be allowed except in a restricted amount. The Bankruptcy Act does not give any power to the Bankruptcy Court to reduce the amount of interest as distinguished from a penalty or forfeiture.

This question is not new but on the contrary was before this Court and determined adversely to the contentions of the Trustees in *Meilink* vs. *Unemployment Reserves Commission*, 314 U. S. 564. In that case it was determined that one per cent (1%) per month charged by the California Unemployment Reserve Act was interest as distinguished from penalty and was not improper. This Court said in that case at page 569:

> "We must give credit to a state legislature acting within its constitutional sphere like that accorded to Congress acting in its constitutional sphere."

Our case is on all fours with the *Meilink* case. The New Jersey Statutes provided (Section 54:27–4):

> "If the taxes of any company, or any portion thereof, remain unpaid on December first following the levying thereof, the company shall be considered in default, and such taxes, or the unpaid portion thereof, shall thenceforth bear interest at the rate of one per cent for each month until paid, notwithstanding the prosecution of a writ of certiorari or other remedy."

Reference to the statute shows that uniformly the charge for interest on account of default is designated as interest and not a penalty. Furthermore there is a provision for penalty in the Act and it is called a penalty. Section 54:23–4 provides for a fixed penalty, regardless of the time element, in the event of the making of a wilful return to the State Tax Department. (There is no question of any such penalty being claimed in this case.) The New Jersey Legislature has strictly maintained the distinction between interest and penalty which is required by the rule laid down in the said *Meilink* case, *supra*.

But in addition, the New Jersey Court of Errors and Appeals in *Wilentz* vs. *Hendrickson,* 135 N. J. Eq. 244, *supra,* has determined that the amount is interest as distinguished from penalty and in arriving at that conclusion cited the just mentioned *Meilink* case (pg. 256).

It follows, therefore, that there is presently no doubt as to the state of the law on the interest question. The *Meilink* case was before the Court below and had that Court not rested its determination on the *Arkansas Corporation Commission* case, it must have found that the Bankruptcy Court was without jurisdiction to make any determination reducing the rate of interest and that the said Court was required to follow the law of the State of New Jersey.

POINT IV.

The argument of the Trustees with reference to the effect of the change in the Railroad Tax Law in 1941 is without merit.

The Trustees have pointed out that by R. S. 54:27–4 (in effect prior to 1941) a lien was given upon the lands and tangible property and franchises of the company in this State. They then point out that the new law in R. S. 54:29A–54 provides that the lien shall be upon,

> "The revenues and all the real and personal property owned, used or controlled by the taxpayer within this State."

The Trustees failed to point out a very necessary part of the Act which provides in Section 54:29A–74 that:

> "This act (chapter) shall be construed as a revision of chapters nineteen through twenty-nine inclusive, of Title 54 of the Revised Statutes, and nothing herein shall be construed to affect any pending litigation, nor

to repeal, abate, cancel, cause to lapse or otherwise affect in any manner any assessment or the lien or obligation to pay any taxes heretofore assessed to any taxpayer, or the legal authority to collect taxes, interest and penalties which have accrued under any provision of law repealed by this act (chapter) or under any other law, except as specifically provided in this act (chapter), or to affect the right of the state tax commissioner to assess omitted property, and apportion the tax so assessed, for any year prior to one thousand nine hundred and forty-one, according to the classification and at the rates prescribed in the chapters aforesaid."

The Trustees, now have for the first time in their present petition to this Court, raised the question that the change in the railroad tax law in 1941 may have caused the State's lien to lapse. Their failure to raise this question during nearly five years of litigation speaks eloquently and is compelling proof of the lack of merit in that contention.

But again we point out that, while throwing out the just mentioned suggestion, the Trustees have shown no power in the Bankruptcy Court to adjudicate such question in a summary manner. Furthermore if the Court should undertake the determination of such matter, it would be bound by the clear provision of the law set out above, which the Trustees, in their brief, failed to mention.

POINT V.

If the Court below had not followed the *Arkansas Corporation Commission* case, it nevertheless must have found that the Bankruptcy Court was without jurisdiction, unless the State should consent thereto, to make adjudications, intended to be binding upon the State, concerning tax liens affixed at the time of bankruptcy.

As we have pointed out, the Court below in its wisdom rested its determination of the jurisdictional question upon a practical exposition of the rule of the *Arkansas Corporation Commission* case as applied to the facts of the instant case instead of upon certain other jurisdictional grounds which would have denied jurisdiction in the Chancery Court to make any adjudication whatsoever concerning the existing tax liens of the State of New Jersey. Since it is our belief that there can be substantial disagreement with the Court below only as to the reasoning for attaining its result and not in anywise with the result itself, we pray the indulgence of this Court in submitting this point which goes rather to the merits of the controversy, for the purpose of showing that a review of this case could only result in an affirmance of the judgment below for the reasons stated by the Court below or an affirmance on one of the grounds now to be set forth.

a. *Section 64 of the Bankruptcy Act does not authorize the Bankruptcy Court to adjudicate concerning the tax liens of the State of New Jersey.*

Section 64 does not apply to tax liens. It applies only to certain priorities given to unsecured claims of persons who except for the said section would have no priority in such assets. *Miners' Savings Bank of Pittston* vs. *Joyce,*

97 F. (2d) 973 (C. C. A. 3rd, 1938); *Ingram* vs. *Coos County*, 71 Fed. (2d) 889 (C. C. A. 9th, 1934); *In re Brannon*, 62 F. (2d) 959 (C. C. A. 5th, 1933), cert. den., 289 U. S. 742, sub. nom. *Ryan* vs. *City of Dallas*; *In re Knox-Powell-Stockton Co.*, 100 F. (2d) 979 (C. C. A. 9th, 1939); *Strom* vs. *Peikes*, 123 F. (2d) 1003 (C. C. A. 2d, 1941); *In re Weil*, 46 F. Supp. 14 (D. C. Pa. 1942); *In re Wilkes-Barre & E. R. Co.*, 46 F. Supp. 12 (D. C. Pa. 1942).

In *In re Brannon*, 62 F. (2d) 959 (C. C. A. 5th, 1933), cert. den., 289 U. S. 742, sub. nom. *Ryan* vs. *Dallas*, the Court stated the rule at page 960:

> "Section 64 gives the rule for paying out the money arising from the bankrupt's property which remains for general distribution after all special liens and encumbrances have been dealt with. * * * On the other hand, where the creditor before the bankruptcy has an established lien on the bankrupt's property which binds it as to third persons and which is not invalidated by the bankruptcy, he does not come under the operation of section 64."

b. *Section 77 does not give the Court jurisdiction to deal with the tax liens of the State.*

Nowhere in Section 77 do we find any mention of taxes. If the Courts had found that Congress intended to include the power to review taxes there would have been no need of reading into the said Section 77 proceedings the provisions of Section 64. The said Section 77 deals with the reorganization of a railroad. All of the definitions stem out of the definition of the word "creditor." This Court and the Courts generally have held that the obligation to pay taxes does not create the ordinary debtor-creditor relationship. It is with such debtor-creditor relationship with which the Congress has dealt in Section 77.

It is admitted that during the time that it is necessary to determine whether or not a railroad will be able to reorganize under private ownership, the officers of a State may be enjoined from foreclosing any equity of redemption. And that is the limit of the power. If it is made to appear when the time comes to submit a plan of reorganization that the taxes will not be paid in full, then the conclusion must be reached that reorganization is hopeless. Congress could never have intended that a State which has been denied its taxes and interest for a considerable period should be required to take securities of railroad companies and go into the railroad business without its consent.

Congress throughout the Bankruptcy Act has consistently demonstrated a policy and purpose to preserve the rights of States and State taxing agencies in the operation of the provisions of the Bankruptcy Act. A construction of Section 77 which would require the State to submit its lien claims to the Bankruptcy Court or have those tax liens wiped out is wholly contrary to such demonstrated policy. We therefore believe that it was not intended that Section 77 should give the Bankruptcy Court power to adjudicate concerning the tax liens of the State of New Jersey which were affixed prior to bankruptcy without the State's consent.

c. *Section 67 does not give the Bankruptcy Court the power to make the requested adjudications.*

The Trustees here for the first time set forth Section 67 as the source of the power to make the requested adjudications concerning the tax liens of the State which were affixed prior to bankruptcy. This debtor filed its petition on October 30, 1939. The taxes for the years 1932 to 1939 became a lien on June 1, of each respective year, the latest

becoming a lien on June 1, 1939, more than four months prior to bankruptcy. It was provided by Section 54:27-4 that:

> "These taxes shall be a lien paramount to all other liens upon all of the lands and tangible property and franchises of the company in this State."

Nothing further was required to be done by the State in order to have the lien attach. That this is so is clearly borne out by Section 54:28-5 providing for sale to enforce the State's tax lien. With respect to property not used for railroad purposes, the Legislature provided as follows:

> "As to any other property of the company or persons, the judgment and execution shall constitute or become liens in the same manner and to the same extent as other judgments and executions of the Supreme Court."

As stated above, the Trustees did not urge the applicability of this section below but raise it here for the first time. It is obvious that since no further action is required by State law to perfect the lien, the said section does not give authority to make the adjudications requested. With reference to the subordinating of the State's lien upon certain personal property for the purpose of paying debts specified in "clauses 1 and 2" having to do with administrative expenses and wages, we point out that, until the need is found for resort to such assets, the question is not properly before the Court. This section discloses clearly that Section 64 does not apply ordinarily in a case where the State does have liens affixed at the time of bankruptcy.

d. ***Since the liens of the State were affixed prior to bankruptcy, the Bankruptcy Court may not make adjudications to be binding upon the State concerning such liens without the State's consent.***

1. ***The Bankruptcy Court may not adjudicate concerning perfected liens without first acquiring jurisdiction over the lienholder.***

It is fundamental that the Bankruptcy Court takes custody of the property of a bankrupt in the same "plight and condition" in which the bankrupt himself held such property at the time of bankruptcy. *Thompson* vs. *Fairbank*, 196 U. S. 516. A trustee takes property of a bankrupt subject to whatever liens existed as against the bankrupt. *Rode & Horn* vs. *Phipps*, 195 F. 414 (C. C. A. 6th, 1912). In *Marshall* vs. *New York*, 254 U. S. 380, 385, the Court said:

> "* * * a receiver appointed by a federal court takes property subject to all liens, priorities or privileges existing or accruing under the laws of the State * * *"

Since the Bankruptcy Court takes property subject to liens, it follows that before the Court can make any adjudications concerning the interest of a lienholder, it must obtain jurisdiction over that lienholder. It was so held in *Factors' & Traders' Insurance Co.* vs. *Murphy*, 111 U. S. 738, where the Court said at page 742:

> "We are of opinion, with the Supreme Court of Louisiana, that the record in this case does not show such service of process or other notice as makes Mrs. Murphy such a party to the bankruptcy proceeding as binds her to the sale and discharges her lien. The case of *Ray* vs. *Norseworthy*, 23 Wall. 128, is conclusive on that subject, and is, we think, sound in principle."

The rule could not be otherwise, else the constitutional rights of a lienholder would be violated. As was said in *Louisville Joint Stock Land Bank* vs. *Radford*, 294 U. S. 553:

> "The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment."

2. *Since it is necessary to obtain jurisdiction over the person of the lienholder, this may not be done where the lienholder is a state unless the state consents.*

In *Arkansas Corporation Commission* vs. *Thompson*, 313 U. S. 132, 145, it was said:

> "But there is nothing in the history of bankruptcy or reorganization legislation to support the theory that Congress intended to set the federal courts up as super assessment tribunals over state taxing agencies."

We do not need to cite authority for the rule that a sovereign state may not be sued without its consent in a Federal Court. A clear statement of the basis for the rule is to be found in *Great Northern Life Insurance Co.* vs. *Read*, 322 U. S. 47, at pages 51 and 54,

What constitutes a suit against a state is not circumscribed within any narrow or technical limits. In *State of Missouri* vs. *Fiske*, 290 U. S. 18, the Court held that the immunity of a State from suit extends to any proceedings wherein process is issued against a state

> "to compel it to subject itself to the court's judgment, whatever the nature of the suit,"

In *Minnesota* vs. *United States,* 305 U. S. 382, a proceeding against property in which the sovereign had an interest was prohibited. In *Worcester County Trust Co.* vs. *Riley,* 302 U. S. 292, a bill of interpleader was held to come within the prohibition.

In *Palmer* vs. *Ohio,* 248 U. S. 32, 34, this Court said:

> "The right of individuals to sue a state in either a federal or a state court, cannot be derived from the Constitution or laws of the United States. It can come only from the consent of the state."

The rule is well stated in *Ex-Parte State of New York,* 256 U. S. 490, wherein it was claimed that the Federal Courts had jurisdiction because an admiralty question was involved. The Court said in *Missouri* vs. *Fiske, supra,* pg. 28.

> "The fact that a suit in a federal court is in rem, or quasi in rem, furnishes no ground for the issue of process against a non-consenting State. If the State chooses to come into the court as plaintiff, or to intervene, seeking the enforcement of liens or claims, the State may be permitted to do so, and in that event its rights will receive the same consideration as those of other parties in interest. But when the State does not come in and withholds its consent, the court has no authority to issue process against the State to compel it to subject itself to the court's judgment, whatever the nature of the suit."

e. *The State has not consented to such suit.*

(1.) *No New Jersey statute or constitutional provision authorizes the participation of the State in Section 77 proceedings in a case where it has liens for its taxes.*

The Trustees have been unable to point to any New Jersey statute or constitutional provision authorizing any officer of the State to consent to the State's participation in these proceedings with respect to its tax liens. No such provision exists. *Strobel Steel Construction Company* vs. *State Highway Commission,* 120 N. J. L. 298. The New Jersey law, as the applicable local law, is conclusive on the subject of consent to be sued. *Palmer* vs. *Ohio, supra.* The State Comptroller was not authorized to prosecute the enforcement of the State's tax liens in this or any other proceeding, nor was he authorized to consent to any adjudication concerning such tax liens.

Since the Comptroller possessed no authority to enforce the lien claims in question, no action by him in these proceedings can be construed as a demand by the State for the enforcement of those liens by this Court. *Minnesota* vs. *U. S., supra; Adams* vs. *Bradley,* 1 Fed. Cases 93, 5 Sawy. 217, 219 (C. C. 1878); *O'Connor* vs. *Slaker,* 22 F. (2d) 147, 152 (C. C. A. 8th 1927); *Title Guarantee & Surety Co.* vs. *Guernsey,* 205 Fed. 94, 95 (D. C. Wash. 1913).

This Court was requested to pass upon the extent of the power of an officer to bind the State in *Ford Motor Company* vs. *Dept. of Treasury of Indiana,* 65 Sup. Ct. Rep. 347 (January 8, 1945). In that case the State's immunity from suit was raised for the first time in this Court.

(2.) *The filing of the proofs of claim merely constituted a notification to the Court and Trustees of the existence and amount of the State's liens and was not a proceeding to enforce the liens.*

It is fundamental in the law of bankruptcy that a claimant must exhaust his security before he can assert a claim against the assets that are in the custody of the Court. *In re Hagin*, 21 Fed. (2d) 434; *New York Trust Co.* vs. *Palmer*, 101 Fed. (2d) 1.

This being the rule and it likewise being the rule that

> "a claim proven as a secured claim is always potentially an unsecured one. If the security fails in whole or in part the equity of the case will generally require that recognition be given the unsecured debt." *McAbee* vs. *Isom*, 116 Fd. (2d) 1001 (C. C. A. 5th 1940.)

the only power that may be attributed to the Comptroller in the instant case has to do with a claim that he may be required to make in the eventuality that the security afforded by the lien should not be sufficient to liquidate the whole tax debt and it should become necessary to make a claim for a deficit.

The Comptroller could not make any estimate as to the amount of any such deficit, since the New Jersey Attorney-General was restrained by the Bankruptcy Court from enforcing the tax liens—the only method given by law whereby the amount of the deficiency claim that the State might ultimately have against the general assets might be proved.

As stated in *Henderson County* vs. *Wilkins*, 43 F. (2d) 670, 672 (C. C. A. 4th, 1930), in speaking of the action of the Court concerning a review of tax claims against the general assets:

> "Its action is not a review of the action of the taxing authorities or a proceeding to enjoin action by them, but a determination under the statute of the amount which should be paid on the claim for taxes from the assets of the estate in its possession. *In re E. C. Fisher Corporation* (*D. C.*), 229 F. 316, 318."

In conclusion of this point, we urge therefore that the Bankruptcy Court did not have the power to make the adjudications requested by the petition of August 14, for the reason that either Congress had not given such power by any provision of the Bankruptcy Act, or if Congress had intended to grant the power to make such adjudications without the State's consent, such grant of power was unconstitutional. Congress was without power to give the Court jurisdiction to make adjudications with respect to tax liens affixed at the time of bankruptcy without the State's consent if such adjudications are intended to be binding upon such State.

CONCLUSION.

It is respectfully submitted that this case involves no matter properly warranting the granting by this Court of the discretionary remedy of review by certiorari and that the prayer for the issuance of the writ of certiorari should be denied.

Respectfully submitted,

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